

OLL 2748/2

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18 Sept 1984

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REMARKS: 1 copy for House Select Committee for Intelligence 1 copy for Senate Select Committee for Intelligence <div style="text-align: center; border: 1px solid black; border-radius: 50%; width: 50px; margin: 20px auto;">2</div>		
FROM: D/OF		
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<small>FORM NO. 241 1 FEB 66</small> <small>REPLACES FORM 36-3 WHICH MAY BE USED.</small>		

STAT

Central Intelligence Agency



Washington, D.C. 20505

DD/A Registry

84-2661/2

LEGISLATIVE LIAISON

84-2748/2

14 SEP 1984

The Honorable Jack Brooks
Chairman
Committee on Government Operations
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

This responds to your request for actions taken or planned by the Central Intelligence Agency regarding your Committee's report on the first year implementation of the Federal Managers' Financial Integrity Act (the Act).

Senior Agency officials have long recognized that the nature of the Agency's mission and the special trust implicit in the grant of unique authorities requires the establishment of strong internal accounting and administrative control systems. Since the Act became law in September of 1982, the Agency has reinforced those systems with the issuance of an "Internal Accounting and Administrative Control Directive." This Directive implements the provisions of the Act and complies with Government Accounting Office standards and Office of Management and Budget guidelines. At this time, the Agency has effected the seven step process for evaluating and reporting on internal control systems. We have evaluated the Agency Accounting System and can affirm that Comptroller General principles, standards, and related requirements for accounting systems have been and will continue to be used as the guidelines against which the system has been developed and is being maintained.

The Committee Report states that a management deficiency should be a material weakness for reporting under the Act if it could impair fulfillment of an agency's mission, deprive the public of needed government services, violate statutory or regulatory requirements, or result in conflict of interest. I agree with that concept. My 1983 report to the President and the Chairmen of the House Permanent Select Committee on Intelligence and the Senate Select Committee on Intelligence did not identify any material weakness. There were none to report. My certification to this effect was based upon the results of an ongoing evaluation, review, and reporting process which enabled me to conclude that the Agency had achieved the optimum accountability possible, within the bounds of practicality, over its total operations.

The Central Intelligence Agency is fully dedicated to the prevention of fraud, waste, and abuse. Our efforts to that end will continue unabated and the status of our internal control and accounting systems will be reported annually to the House Permanent Select Committee on Intelligence and the Senate Select Committee on Intelligence.

Sincerely,

/s/ William J. Casey

William J. Casey
Director of Central Intelligence

SUBJECT: Reply to Letter from Congressman Jack Brooks
Federal Managers' Financial Integrity Act

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ROUTING AND RECORD SHEET

SUBJECT: (Optional)

Reply to Letter from Congressman Jack Brooks
Federal Managers' Financial Integrity Act

FROM:

Harry E. Fitzwater
Deputy Director for Administration
7D 24 Hqs

EXTENSION

NO.

DDA 84-2661/2

DATE

11 September 1984

STAT

TO: (Officer designation, room number, and building)

DATE

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COMMENTS (Number each comment to show from whom to whom. Draw a line across column after each comment.)

1. Executive Registry

2. OLL
ATTN: [redacted]

11 SEP 1984

12 SEP 1984

SDR

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3. Executive Director

4. Deputy Director of
Central Intelligence

9/13

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5. Director of Central
Intelligence

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14 SEP 1984

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attached is a letter to Congressman Brooks reporting on our "First-Year Implementation of the Federal Managers' Financial Integrity Act." When the Act was passed we determined that our controls and accounting systems complied with the requirements of the Act. This letter reports that we have complied with the Act and had no problems during the past year.

STAT

STAT

INSPECTOR GENERAL

84-599/1

ROUTING AND RECORD SHEET

SUBJECT: (Optional)

Federal Manager's Financial Integrity Act

DD/A Registry

84-2661/1

FROM:

EXTENSION

NO.

Acting Inspector General

DATE

4 September 1984

TO: (Officer designation, room number, and building)

DATE

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COMMENTS (Number each comment to show from whom to whom. Draw a line across column after each comment.)

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DDA/EXO

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I think this is more appropriately a response from the Office of Finance. We (IG and Audit) provide technical advice and prepare the annual report based upon DD certifications. I think this is not a big deal, but we probably should give Brooks the courtesy of a response. Sorry for the time limitation. I just got this this a.m. [redacted] folks worked on last year's submission.

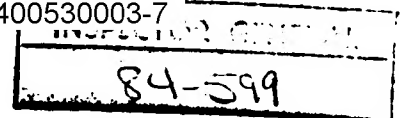
#4 - For Action
Send Response via the DDA

Suspense!

7 September 1984

Great

OLL 84-2748/1
30 August 1984



MEMORANDUM FOR: Chief, Audit Staff
Office of Inspector General

Chief, Administrative Law Division
Office of General Counsel
Attn:

STAT

FROM:



Chief, Legislation Division
Office of Legislative Liaison

STAT

SUBJECT: Federal Manager's Financial Integrity Act

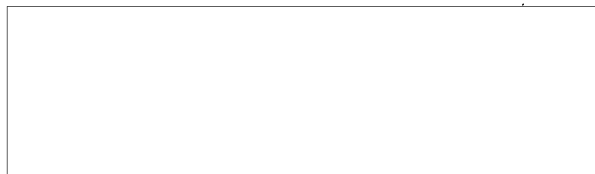
1. Attached for your review is a letter from Congressman Jack Brooks, Chairman of the House Government Operations Committee, enclosing a report entitled "First-year Implementation of the Federal Manager's Financial Integrity Act." Chairman Brooks requests in this letter that the Agency report on actions planned or taken in response to the report's recommendations.

2. I would appreciate your reviewing the attached report carefully to determine if an Agency response is necessary, and the form that response should take. As the Committee has asked us to respond by 7 September 1984, your prompt attention to this matter is requested.

3. Please do not hesitate to call if I can be of further assistance.

STAT

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Attachment

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Congress of the United States House of Representatives

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MAJORITY—225-5051
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August 7, 1984

Executive Registry

84-1509/E

LEGISLATIVE LIAISON

84-2118

Honorable William J. Casey
Director
Central Intelligence Agency
Washington, D.C. 20505

Dear Mr. Casey:

Enclosed is a copy of the report approved by the Committee on Government Operations entitled "First-Year Implementation of the Federal Managers' Financial Integrity Act."

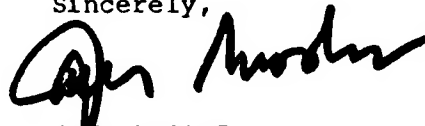
The report is a result of the Legislation and National Security Subcommittee's review and May 22, 1984 hearing concerning the Federal government's efforts to implement the Act. It provides the Committee's views regarding Federal agencies' progress made and problems encountered during the first year. Also discussed are potential obstacles to the Act's full implementation.

The report contains recommendations requiring action by your agency to help assure that the Act is fully implemented so that the maximum possible improvement in the management of Federal programs and operations can be achieved. Agency heads are required to take actions to assure that all programs and functions are covered, assure that all material weaknesses are properly recorded and reported, complete the evaluation process, and correct internal control and accounting system weaknesses.

I would appreciate your advising the Committee within 30 days as to the actions you have taken or plan to take in response to the report's recommendations. Additional copies of the report are available if you desire to distribute the Committee's views to managers throughout your agency.

With best wishes, I am

Sincerely,



JACK BROOKS
Chairman

Enclosure

Union Calendar No. 536

98th Congress, 2d Session - - - - - House Report 98-937

**FIRST-YEAR IMPLEMENTATION OF THE FEDERAL
MANAGERS' FINANCIAL INTEGRITY ACT**

FORTY-THIRD REPORT

BY THE

**COMMITTEE ON GOVERNMENT
OPERATIONS**



**AUGUST 2, 1984.—Committed to the Committee of the Whole House on the
State of the Union and ordered to be printed**

U.S. GOVERNMENT PRINTING OFFICE

36-998 O

WASHINGTON : 1984

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LETTER OF TRANSMITTAL

HOUSE OF REPRESENTATIVES,
Washington, DC, August 2, 1984.

Hon. THOMAS P. O'NEILL, Jr.,
Speaker of the House of Representatives,
Washington, DC.

DEAR MR. SPEAKER: By direction of the Committee on Government Operations, I submit herewith the committee's forty-third report to the 98th Congress. The committee's report is based on a study made by its Legislation and National Security Subcommittee.

JACK BROOKS, *Chairman.*

(III)

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(v)

Union Calendar No. 536

98TH CONGRESS }
2d Session

HOUSE OF REPRESENTATIVES

{ REPORT
98-937

FIRST-YEAR IMPLEMENTATION OF THE FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT

AUGUST 2, 1984.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. BROOKS, from the Committee on Government Operations,
submitted the following

FORTY-THIRD R E P O R T

BASED ON A STUDY BY THE LEGISLATION AND NATIONAL SECURITY
SUBCOMMITTEE

On July 31, 1984, the Committee on Government Operations approved and adopted a report entitled "First-Year Implementation of the Federal Managers' Financial Integrity Act." The chairman was directed to transmit a copy to the Speaker of the House.

I. SUMMARY

The Federal Managers' Financial Integrity Act (the Act) became law in September 1982, following continuing disclosures of fraud, waste, and abuse associated with weak internal control and accounting systems. Such abuses have hampered the Federal Government's effectiveness and accountability, and eroded the public's confidence. The Act requires Federal managers, for the first time, to establish a continuous process for evaluating, improving, and reporting on the internal control and accounting systems for which they are responsible. It thus reaffirms the requirements of the Accounting and Auditing Act of 1950, which place the primary responsibility for establishing and maintaining effective internal control and accounting systems on the Federal Government's managers. The term "internal controls," as envisioned by the Act, is synonymous with "management controls" and clearly encompasses program and administrative areas, as well as the more traditional accounting and financial management areas.

In compliance with the Act's requirements, the General Accounting Office promulgated standards for agencies to use in establish-

36-998 O

ing and maintaining their internal control systems, and the Office of Management and Budget issued guidelines to direct the agencies' internal control evaluation, improvement and reporting process. Federal agency managers have begun to put in place an evaluation system for their internal control and accounting systems. Based on this limited evaluation, Federal agency heads have also submitted their first annual reports to the President and the Congress, as required by the Act. Internal control and accounting system weaknesses disclosed in these reports can be categorized into eight major areas covering all aspects of government operations. The weaknesses identified in the Federal agencies' first year reports, even though the reports are based on limited agency evaluations, and are, therefore, likely to have excluded other major areas of weakness, are an indication of the breadth and magnitude of the existing problems in the Federal Government's internal control and accounting systems. The weaknesses already identified, and those weaknesses which may be identified as agencies complete the evaluation process, must be remedied if the Act is to be fully successful in restoring the public's confidence in its government's ability to manage itself effectively.

Much remains to be done to complete the evaluation and reporting process, and to correct identified problems. While progress has been significant as a result of the evaluation efforts begun this year, some problems with agency implementation efforts have already been identified. Further, there are several potential problems which if not addressed, may prevent the Act from being fully implemented. Problems agencies encountered in different aspects of the implementation process, such as guidance, reporting, scope of implementation, documentation, training, automated data processing control reviews, and accounting system evaluations, have already been identified. Agencies have generally agreed to correct deficiencies in their implementation processes in future years' efforts to implement the Act. Misperceptions that the Act merely adds to managers' paperwork burden, that the Inspectors General should be responsible for managerial functions, that managers need not be committed to the Act's full implementation, and that financial management reforms need not be coordinated with the on-going work under this Act, are all concerns which agency managers must address if the Act is to be effectively implemented.

Federal agency managers need to build on the work done this year. They must complete their detailed internal control and accounting system reviews, and take appropriate actions to correct weaknesses identified.

II. INTRODUCTION

Federal managers have now had over one full year in which to begin implementing the requirements of the Federal Managers' Financial Integrity Act. The Act was signed into law on September 8, 1982, following disclosures that weak internal control and accounting systems often lead to fraud, waste, and abuse. The Act places primary implementing responsibility on Federal managers, but it also mandates specific actions by the Office of Management and Budget and the General Accounting Office.

In order to review the progress and problems encountered after one full year's implementation of the Act, the Legislation and National Security Subcommittee held a hearing on May 22, 1984. Appearing before the Subcommittee were Charles A. Bowsher, Comptroller General of the U.S. General Accounting Office (GAO), and Joseph R. Wright, Jr., Deputy Director, Office of Management and Budget (OMB).

III. THE FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT

A. BACKGROUND

The head of each executive agency has been required by law to establish and maintain adequate systems of accounting and internal control since passage of the Accounting and Auditing Act of 1950. While many worthwhile improvements in the Federal Government's internal control and accounting systems have been undertaken during the intervening 30 years, continuing reports of fraud, waste and abuse have served to underline the need for further management attention—to establish controls where none are in place, strengthen existing controls and accounting procedures where necessary, and assure that control and accounting procedures are followed by agency personnel.

The Federal Managers' Financial Integrity Act is intended to provide the impetus to assure that Federal managers devote the necessary attention to this endeavor. It builds upon the requirements of the 1950 Act. While reaffirming management's responsibility for internal controls, it adds the discipline necessary for managers to identify and remedy problems in internal control systems, both financial and management, that are sometimes longstanding and that hamper effectiveness and accountability.

Agency heads are now required to establish a continuous process for the evaluation and improvement of the internal control systems for which they are responsible, and to publicly account for the status of their internal control and accounting systems.

B. REQUIREMENTS

The Act (see appendix) contains separate requirements for Federal agency internal control systems (Section 2) and accounting systems (Section 4). Section 2 requires that agency internal control systems be evaluated to determine if they comply with the Act's three objectives:

- Obligations and costs are in compliance with applicable law;

- Funds, properties and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and

- Revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the assets.

The Act places full responsibility for agencies' internal control systems on agency heads by requiring that they submit annual reports to the President and the Congress on whether their internal control systems fully comply with these objectives. Each report must include a description of any material internal control weaknesses identified through the assessment process, along with plans to correct such weaknesses.

To help clarify managers' internal control responsibilities, the Act requires the Comptroller General to prescribe internal control standards and the Director of the Office of Management and Budget to establish guidelines for evaluating, improving, and reporting on internal controls. Accordingly, the Comptroller General promulgated "Standards for Internal Controls in the Federal Government" in June 1983. These standards are to be met by Federal agencies in establishing and maintaining their systems of internal control. The Director of the Office of Management and Budget, after consulting with the Comptroller General, issued a document entitled "Guidelines for Evaluation and Improvement of and Reporting on Internal Control Systems in the Federal Government," in January 1983. These guidelines suggest an approach to agency management "self assessment" evaluation and improvements as the basis for the required annual statements on the status of their internal control systems.

Section 4 of the Act requires that agency heads provide separate annual statements on whether their accounting system conforms to the Comptroller General's Accounting Principles and Standards.¹ The Act does not require the development of guidance for agency heads' use in evaluating and reporting on the extent of their accounting systems' compliance. However, in September 1983 the Comptroller General did suggest a number of steps agencies could take during the first year to provide a building block for more thorough accounting system evaluations in future years.²

Section 2 is now codified as 31 U.S.C. 3512; Section 4 is 31 U.S.C. 3512(c)(2)(B).

C. WHAT ARE INTERNAL CONTROLS?

Although the Act relates to all management functions, many of the terms used in the Act and the resulting standards and guidelines have been borrowed from the accounting discipline. That discipline has developed a vocabulary of words and phrases which, over the years, through usage, judicial decisions, and other means have acquired recognized and accepted meanings within the accounting profession. As a result, the meaning of the term "internal

¹ GAO's Policy and Procedures Manual for Guidance of Federal Agencies contains the principles, standards, and related requirements to be observed by Federal agencies in establishing and maintaining accounting systems. Specifically, Title 2 prescribes the overall accounting principles and standards, while Titles 4, 5, 6, and 7 specify requirements governing claims; transportation, pay, leave and allowances; and fiscal procedures.

² The Comptroller General's September 29, 1983, speech before the President's Council on Integrity and Efficiency outlined the following steps: (1) organize the accounting system evaluation process, (2) develop an inventory or list of accounting systems, (3) identify previously reported deviations from the Comptroller General's requirements, (4) identify any projects underway to enhance accounting systems, (5) rank the systems based on how material the deviations might be, (6) begin reviewing the systems to find out if they comply with the requirements, and (7) plan for the first-year report.

controls" is sometimes difficult to understand for those with little or no background in the field of accounting or financial management.

Internal controls, as envisioned by the Act, encompass the program management and administrative areas, as well as the accounting and financial management areas, of agency operations. The Comptroller General's Standards for Internal Controls in the Federal Government clearly provide that internal controls are intended to cover all management functions in the Federal executive departments and agencies.³

Traditionally, internal controls have been classified into two categories: internal accounting controls and internal administrative controls. Under this classification, accounting controls are concerned with safeguarding assets and assuring the accuracy and reliability of accounting transactions and reporting. Administrative controls are concerned with assuring adherence to prescribed managerial policies and promoting operational efficiency.

The terms "internal controls" and "management controls" are synonymous. Internal controls are inherent in the management function. That is, internal controls are integral to all systems (whether related to administration, program operations or accounting) used by management to achieve the objectives of programs or functions. An internal control, whether "accounting" or "administrative" in nature, can be most readily understood as a combination of a control objective and the technique(s) or procedure(s) used to achieve that objective. In the accounting control area, for example, an objective may be to safeguard a petty cash fund. A technique that may be used to provide reasonable assurance that this objective is accomplished is to assign responsibility for authorizing disbursements from the fund to someone other than the individual responsible for maintaining custody of the fund. Other techniques that may be used are to maintain the fund in a locked safe, to restrict access to the safe to a few people, and to require that the safe's combination be changed periodically. Management would utilize as many techniques as necessary, commensurate with the risk of loss.

In the administrative control area, an example of a control objective in a program area is that all military forces be maintained in a state of readiness commensurate with strategic plans. Techniques that may be used to provide reasonable assurance that our military is sufficiently ready to defend against attack are (1) definition of readiness requirements for each military unit, (2) provision of readiness training, and (3) periodic testing and reporting against readiness requirements.

³ The Standards define internal controls as: the plan of organization and methods and procedures adopted by management to ensure that resource use is consistent with laws, regulations, and policies, that resources are safeguarded against waste, loss, and misuse, and that reliable data are obtained, maintained and fairly disclosed in reports.

IV. FIRST YEAR PROGRESS

A. AGENCY ACTIVITIES

Most agencies appear to be progressing toward full implementation of the Act. While much has been accomplished in the first year, there is a need for even greater efforts to be made. The guidelines issued to assist agency managers in implementing the Act detail a seven step process for evaluating, improving, and reporting on agency internal control systems.⁴ Most Federal agencies, however, made only limited progress beyond the third step of that process, i.e., conducting assessments of the vulnerability of specific units to loss of resources, mismanagement, waste, etc. Managers in the agencies that have made progress beyond the vulnerability assessment step have begun detailed internal control reviews based primarily on the ranking of agency vulnerability assessments. That is, the most vulnerable areas receive first priority in scheduling internal control reviews. These detailed reviews, which include testing existing controls to determine their adequacy, are designed to identify specific internal control weaknesses. For example, the Department of Education reported that 48 internal control reviews were completed in 1983 out of 112 assessable units included in the Department's action agenda. Other agencies conducted pilot studies to determine that best method for conducting internal control reviews in their agencies, or incorporated the requirements of the Act into already ongoing reviews of internal controls.

Only very limited efforts have been undertaken to evaluate agency accounting systems, apparently due primarily to the lack of specific guidance to assist managers in complying with the section 4 requirements of the Act. Most agencies, however, have attempted to identify the accounting system(s) subject to the reporting requirement. In addition, many agencies made an effort to comply by using checklists or questionnaires to determine if their accounting system(s) conform to the Comptroller General's accounting principles and standards. (See subsequent report section "Accounting Systems Evaluations" for a discussion of the Committee's view in this area.)

Considerable differences in the approaches agency managers have taken to implement the Act have resulted because of the variations in agency size, mission, and existing organizational and management structure. The number of assessable units agencies identified during the first year effort provides an illustration of the variation in implementation approaches used. The Department of Health and Human Services, for example, identified 6,238 internal control areas for which it conducted vulnerability assessments.⁵ In another instance, the Department of the Army managers reported assessing risks on about 45,000 units.⁶ At the other extreme, the

⁴ The seven steps are: (1) organizing, (2) segmenting agency functions into assessable units, (3) assessing vulnerability, (4) planning for subsequent reviews, (5) reviewing internal controls, (6) taking corrective actions, and (7) reporting.

⁵ GAO Report, "The Department of Health and Human Services' First-Year Implementation of the Federal Managers' Financial Integrity Act," HRD-84-47, May 9, 1984.

⁶ GAO Report, "Department of the Army's First-Year Implementation of the Federal Managers' Financial Integrity Act," NSIAD-84-92, May 1, 1984.

Department of the Navy's initial set of vulnerability assessments was conducted on 20 broad-based programs and functions,⁷ which it had identified as assessable units. It should be noted, however, that these numbers, in and of themselves, are not a reliable indicator of the quality of an agency's vulnerability assessment process. That is, a large number of assessable units does not necessarily indicate a "good" process, or conversely, a small number of assessable units is not a reliable measure of a "poor" process. Rather, the propriety of the number of vulnerability assessments a given agency performs must be judged in light of the agency's size, mission, programs, and organizational structure, and the potential improvement which might be made as a consequence of the choice of assessable units.

Agencies used the internal control evaluations as a basis for their annual reports to the President and the Congress on the status of their internal control systems, and their plans for corrective action. The first year reports identified weaknesses in agency-wide functions and operations as well as in specific program activities.

Material weaknesses in internal control systems reported by the agencies have been divided into eight categories. The number of agencies reporting weaknesses in each category is depicted in the following chart:⁸

Categories of material weaknesses reported by agencies GAO reviewed (as of Dec. 31, 1983)

Functional area:	Agencies ¹
1. Accounting and financial management.....	16
2. Eligibility and entitlement.....	8
3. Grant, loan, and debt collection management.....	12
4. Procurement.....	14
5. Property management.....	13
6. Automated data processing.....	10
7. Cash management.....	13
8. Personnel and organizational management.....	10

¹ Number of agencies reporting weaknesses in area: The GAO's review included 17 separate departments and independent agencies, including the Department of Defense [DOD]. Separate reports were issued for all 17 agencies and for 5 components within DOD—a total of 22 reports.

The weaknesses reported cover all aspects of government operations. Many of them are not newly discovered, however, as they have been the subject of prior reports issued by GAO and by the agencies' Inspectors General. For example:

The Interior Department reported material weaknesses in its multibillion dollar oil and gas royalty program, including the lack of timely royalty payment deposits and the lack of on-site auditors assigned to the top 20 royalty payors. GAO has issued numerous reports dating back 25 years addressing problems in accounting for oil and gas royalties.

The Department of Defense identified its foreign military sales program as an area of material weakness. DOD cited a need to ensure that all sales are made in accord-

⁷ GAO Report, "Department of the Navy's First-Year Implementation of the Federal Managers' Financial Integrity Act," NSIAD-84-94, May 1, 1984.

⁸ Subcommittee hearing.

ance with the Arms Control Act and that there is a proper accounting for U.S. resources and customer funds. In this area, GAO has issued over 40 reports in the last decade identifying hundreds of millions of dollars of excess costs to the Government.

The Department of Defense also disclosed material weaknesses in controls over the procurement of spare parts. Prior GAO and Inspector General reports have reported Defense paying excessive amounts for parts.

The Department of Agriculture reported material weaknesses in its \$11 billion Food Stamp program, including problems in certification, quality control, and detection and collection of overissuances. GAO previously reported that food stamp costs incurred as a result of errors or fraud, could have provided benefits to about 1.7 million needy people for 2 years.

Overall, first-year efforts to implement the Act can be characterized as a learning experience. Agencies did begin the required evaluations and submitted their first reports; however, much remains to be done to complete the evaluation and reporting process and to correct identified problems. The work this year provides the foundation upon which agencies can systematically allocate resources, in a cost-effective way, to perform future evaluations required to identify specific control weaknesses and take appropriate corrective actions. Agency managers' complete and thorough implementation of all seven steps of the guidelines is critical to the success of the Act.

B. OMB, GAO, AND IG ACTIVITIES

The first year's implementation of the Act was notable for the efforts of both the Office of Management and Budget (OMB) and the General Accounting Office (GAO) to establish a framework for the Act's implementation. The two agencies fulfilled their responsibilities under the Act—GAO was required to issue standards for all agencies to use in establishing and maintaining systems of internal control; and OMB was required to issue guidelines for agencies to use in evaluating, improving, and reporting on their systems of internal control. They also maintained oversight of the agencies' activities and provided central direction, training, and technical assistance.

OMB established an interagency task force to provide technical assistance, facilitate information exchange concerning promising evaluation methods and techniques, and monitor agency progress. OMB also sponsored seminars and training sessions to help assure that agency personnel understood the requirements of the Act and its implementing guidelines.

The GAO has similarly demonstrated a significant commitment to assuring the Act's successful implementation. The GAO undertook a comprehensive review of efforts to implement the Act at 22 Federal departments and agencies, which together account for over 95 percent of all Federal expenditures. GAO is currently issuing individual reports to each of the 22 agencies reviewed, and plans to issue an overall report on their first-year review efforts. These re-

ports contain recommendations to help individual agencies correct problems with implementation efforts. For example, GAO has reviewed and made suggestions regarding the initial set of assessable units, on an agency-by-agency basis. In general, agencies have agreed to take the necessary actions to correct the implementation problems GAO has identified.

The Inspectors General have also made significant contributions to the Act's implementation. OMB's guidelines suggest three potential roles that an agency Inspector General may adopt to assist managers in implementing the Act: (1) providing technical assistance to management, (2) commenting on the adequacy of management's implementation process, and (3) conducting their own reviews of internal controls. All of the Inspectors General and the nonstatutory audit organizations in the 22 departments and agencies reviewed by GAO performed at least one, if not all three of the roles recommended by the guidelines.

The expertise and organizational status of the Inspectors General combine to place those officials in a unique position to provide technical assistance, quality assurance, and independent review and oversight for management. The Committee encourages the Inspectors General to continue to assist in the implementation process consistent with the degree of independence needed to fulfill the requirements of the Inspector General Act of 1978. (See subsequent report section, "Inspectors General Role" for a more detailed discussion of the Committee's views on this issue.)

V. AREAS NEEDING IMPROVEMENT

Federal agencies' year-end reports provide for the first time a list of material weaknesses in each agency, and progress toward corrective action as a result of the evaluation efforts has been significant. However, problems have been identified in the areas of guidance, reporting, scope of implementation, documentation, training, controls over automated data processing, and accounting system evaluations.⁹ These problems are discussed in the following sections. The Committee urges the agencies to carefully review their implementation procedures in consultation with GAO and OMB. The review should help in determining where procedures have been deficient and in correcting deficiencies in the process as part of their second year implementation efforts.

A. PRACTICAL GUIDANCE FOR MANAGERS

The Committee believes that complete and consistent understanding of the terms used in the Act and its implementing guidance should be central to achieving the improvements envisioned by the Act. As mentioned previously, the terms and concepts used in the Act were adopted from the accounting discipline. The standards and guidelines have merely repeated these terms without defining them in a manner more readily understandable by line managers. Managers, many of whom are unfamiliar with the terms are now expected to understand them. More practical, detailed guidance is needed for use by managers in determining what consti-

⁹ Testimony of Mr. Bowsher, hearing.

tutes reasonable assurance, a material weakness, a vulnerability assessment, an internal control and an internal control review. The Committee believes that existing guidance should be reexamined with a view to providing more readily understandable definitions for program managers.

The Committee recognizes that the first year's implementation efforts constituted a learning experience for government managers. The Committee believes, however, that the terminology used in the Act and its implementing guidelines and standards should be reexamined with a view to providing more readily understandable definitions for program managers. Only in this way will the evaluation, improvement and reporting procedures required by the Act become part of management's day-to-day procedures.

B. REPORTING PROBLEMS

While agencies' reports disclosed significant weaknesses, the coverage of the reports submitted by several agencies is subject to question. For example, while the Department of Health and Human Services (HHS) reported over 200 material weaknesses identified through internal control reviews, it did not report several other significant internal control problems that had been previously identified by GAO and the HHS Inspector General. These unreported problems appear to be more material than many of the weaknesses disclosed in the HHS year-end report filed in compliance with the Act. HHS did not report weaknesses in the—

Social Security Administration's benefit claims processing procedures. (GAO previously identified about 2.1 million instances in which two or more people had the same social security number, and over \$125 million in erroneous benefit payments.)

Social Security Administration's entitlement and benefit payment programs. (GAO previously reported weaknesses in maintaining accurate social security wage data as a result of SSA's failure to prevent employers from submitting erroneous wage data.)

Health Care Financing Administration's (HCFA) payments for beneficiary medical services. (GAO previously reported that HCFA's internal controls were inadequate to prevent payments for medically unnecessary services.)¹⁰

Concerns have also been raised with respect to the year-end report of the National Aeronautics and Space Administration (NASA).¹¹ NASA did not disclose any material internal control weaknesses in its report to the President and the Congress. However, NASA's own internal review activities reported several problems which "may indicate material weaknesses." For example, the Assistant Administrator for Procurement identified material weaknesses in such areas as procurement management, pre-contract award, and bid contract administration. The Administrator of

¹⁰ GAO Report, "The Department of Health and Human Services' First-Year Implementation of the Federal Managers' Financial Integrity Act," HRD-84-47, May 9, 1984.

¹¹ GAO Report, "National Aeronautics and Space Administration's First-Year Implementation of the Federal Managers' Financial Integrity Act," NSIAD-84-100, May 1, 1984.

NASA did not judge these weaknesses to be of sufficient importance to be brought to the attention of the President or the Congress. In another instance, functional reviews done in 1982 by NASA's own internal review personnel at three different NASA centers disclosed that these centers had incurred costs in excess of obligational authority, indicating that NASA has committed the Government to the expenditure of funds without Congressional approval. NASA's functional review teams reported that this practice could represent a violation of the Anti-Deficiency Act.¹² Despite the apparent seriousness of this problem, the Administrator judged it not to be "material" to the President or the Congress.

Although an assessment of the year-end reports must take into account the incomplete implementation upon which they are based, the above examples indicate obvious omissions of problems which had been the subject of previous internal reviews or GAO reviews and which have not yet been corrected. The Committee believes that deficiencies should be included in the reports issued by agency heads, even if the deficiencies have been previously reported. Full disclosure by the agencies is essential to achieve the improved internal controls throughout the executive branch anticipated by the Act.

Moreover, the Committee is concerned with the lack of consistency in agencies' implementation of the reporting requirements. Consistent understanding of the meaning of material weakness and full reporting of material weaknesses is central to achieving the accountability envisioned by the Act. The Committee believes that a management deficiency should be considered a material weakness for purposes of reporting under the Act if it could impair fulfillment of an agency's mission, deprive the public of needed government services, violate statutory or regulatory requirements, or result in a conflict of interest.¹³

The Committee questions whether the term "reasonable assurance" has been used consistently, and whether meaningful reporting has resulted from the term's application. Even though agency managers were not able to complete the full internal control review process this year, most reported that they had reasonable assurance that their internal controls were adequate simply on the basis of their overall thoughts and opinions of their internal control and accounting systems.

In addition, a more informative reporting format would be useful for those agencies that believe they have reasonable assurance that their internal controls were adequate for part, but not all of their operations. In their first year reports under the Act, agency heads

¹² This Act (31 U.S.C. 1341) prohibits officers or employees of the United States Government from making or authorizing an expenditure or obligation exceeding an amount available in an appropriation. An officer or employee who knowingly or willfully violates this prohibition is subject to either a \$5,000 fine or two years' imprisonment, or both.

¹³ This concept of materiality should not be confused with that used by the accounting profession in conjunction with financial statements. In the accounting profession materiality is defined in financial terms. The AICPA audit standard for use by independent accountants in conjunction with reporting on their review of an entity's system of internal accounting control provides that: "A weakness is material if the condition results in more than a relatively low risk of such errors or irregularities in amounts that would be material in relation to financial statements." That is, all deficiencies which are so significant that they may influence a third party's judgment as to the financial position of the entity being reviewed are considered material and should be disclosed.

were required to state either "yes, my controls taken as a whole provide reasonable assurance" or "no, my controls taken as a whole do not provide reasonable assurance." The Committee is concerned whether agencies such as the HHS, which reported 200 material weaknesses, can legitimately report that, taken as a whole, there is reasonable assurance that its internal controls are adequate. A middle ground reporting option may be necessary to permit agencies to state that they "have reasonable assurance (or are in compliance with the accounting principles) in all areas except . . ." and then list the areas in which they do not have reasonable assurance, or are not in compliance. This approach would have been more practical for a department such as HHS, for example, and would have resulted in a more informative year-end statement.

Further, agencies seem to be reporting only matters which the agencies determine to be matters of significance to the President and the Congress. Apparently, this interpretation is based on OMB guidelines which outline as one of the steps in the implementation process that a senior official should determine whether any material weakness of significance to the President and the Congress was uncovered and if there were, "a brief description should be obtained along with the plans and schedule for correcting the weakness. This information would be incorporated into the report." This interpretation is, in the Committee's view, incorrect. The Act is intended to provide the necessary discipline to discover and correct internal control and accounting deficiencies. The question of which deficiencies should be reported is central to the government's ability to restore full accountability throughout its operations, and to demonstrate to the public that its government is able to effectively manage the resources entrusted to it. With this in mind, the Committee suggests that a more useful interpretation of the Act's requirement to report "material weaknesses" is that if a problem is significant to a program or individual agency component, it should be considered a major problem for the department or agency, and should be reported to the President and the Congress.

In order to assure the integrity of the reporting process, the Committee plans to monitor future agency year-end statements closely to determine if agencies are disclosing all known material weaknesses and if the reporting format is sufficiently informative. All agencies should institute procedures to assure that all material internal control weaknesses are properly recorded and reported as part of their second year evaluation process.

C. SCOPE OF IMPLEMENTATION

With respect to the scope of implementation (that is, the inclusiveness of an agency's operations in its implementation efforts), questions have been raised as to whether agency implementation processes are sufficiently comprehensive. The guidelines for the Act's implementation clearly provide that the foundation upon which the entire internal control evaluation process builds is an agency-wide inventory of "assessable units," which provides complete coverage of all program and administrative functions. The only exclusion provided for under the guidelines is for functions

dealing with "statutory development or interpretation, determination of program need, resource allocation, rulemaking, or other discretionary policymaking processes in an agency."

This provision has been used by some agencies to omit functions which should have been included in the internal control evaluation process. For instance, the Department of the Treasury excluded the \$13 billion Exchange Stabilization Fund¹⁴ from its evaluation process. The Committee recognizes that policies underlying Government operations in the international area have traditionally been excluded from audit.¹⁵ The Act, however, does not require an audit of the Fund, nor does it require evaluation of the *policy* behind governmental actions involving the Exchange Stabilization Fund; that is why the Government may have bought currency from an individual country. Nevertheless, there is a need to determine whether effective controls are in place to assure the safety and appropriate management of the government's resources in this functional area. Chairman Brooks emphasized that the Exchange Stabilization Fund should be subject to the evaluation, improvement, and reporting requirements of the Act:

We are not asking for policy judgmental evaluations. We are asking for basic accountability and for evaluation of areas that might be vulnerable in a \$13 billion operation.

Another example of insufficient coverage is the National Aeronautics and Space Administration's inventory of internal control systems.¹⁶ NASA's inventory did not include all agency programs and functional areas. In reporting on her review of NASA's implementation of the Act, the NASA Inspector General stated that:

Since the assessable unit inventory serves as the foundation on which a complete and thorough implementation rests, I believe that NASA management should reevaluate the adequacy of the currently identified inventory to meet the full intent of OMB's guidelines.

The Committee recommends that all agencies review their inventory of assessable units to assure complete coverage of all programs, systems, and operations.

Efforts by agency managers to protect certain functions from review are misguided at best. The Committee urges all agency managers to cease efforts to secrete any program or activity from review and also urges agency managers to view this Act as a way to strengthen government management across the board, as the Congress intended.

¹⁴ The Exchange Stabilization Fund enables the Secretary of the Treasury to deal in gold and foreign exchange and other instruments of credit and securities regarding orderly exchange requirements.

¹⁵ Testimony of Mr. Bowsher, hearing.

¹⁶ GAO Report, "National Aeronautics And Space Administration's First-Year Implementation of the Federal Managers' Financial Integrity Act," NSIAD-84-100, May 1, 1984.

D. DOCUMENTATION

Another problem area in agency implementation efforts is documentation.¹⁷

The documentation developed by the agencies during the first year was generally inadequate to support their conclusions regarding the adequacy of their internal control systems. For example, the Department of the Air Force lacked documentation of the methods used, and the rationale for conclusions reached in both its initial vulnerability assessments and internal control reviews.¹⁸

The Act's implementing guidelines specify that Federal agencies should maintain adequate documentation for all phases of their evaluation process, including what functions or programs were assessed, how and by whom evaluations were performed, and the rationale for conclusions reached. Documentation is essential to the Act's full implementation because it allows managers and oversight personnel to determine the adequacy of an agency's evaluation process. Recommendations for improved documentation have been made by the GAO in reports based on reviews conducted in individual agencies. If these recommendations are adopted, agencies should be able to demonstrate significant improvement in this area in future years.

E. TRAINING

A fifth problem is training. In some agencies, personnel assigned responsibility for the evaluation of internal controls received no training at all. In other agencies, training was provided too late to be of benefit to managers in this year's internal control evaluation process, or the training merely provided an overview or introduction to internal controls without including any training in the methods and procedures managers should use to meet the requirements of the Act. Examples of insufficient training are found at the Departments of State and Education. At least 50 percent of the people who performed assessments at the Department of State,¹⁹ and 45 percent at the Department of Education,²⁰ received no training. Additionally, many of the 45,000 vulnerability assessments and 8,300 internal control reviews conducted by the Department of the Army were either inadequate or inconsistent because of the lack of specific guidance and training material.²¹

Proper training can play an important role in successful implementation of the Act. Training can help managers to better understand the largely unfamiliar concepts and self-assessment procedural requirements of the Act. The Office of Management and Budget,

¹⁷ GAO's report on the Air Force's Implementation of the Act (NSIAD-84-93, May 1, 1984) defines documentation as: that information which would allow an independent reviewer to reach the same conclusions as the original reviewer regarding an agency's internal controls; and the methods used, personnel involved, and conclusions reached in conducting its internal control evaluation, improvement, and reporting process.

¹⁸ GAO Report, "Department of the Air Force's First-Year Implementation of the Federal Managers' Financial Integrity Act," NSIAD-84-93, May 1, 1984.

¹⁹ GAO Report, "Department of State's First-Year Implementation of the Federal Managers' Financial Integrity Act," NSIAD-84-91, May 1, 1984.

²⁰ GAO Report, "First Year Implementation of the Federal Managers' Financial Integrity Act by the Department of Education," HRD-84-49, May 9, 1984.

²¹ GAO Report, "Department of the Army's First-Year Implementation of the Federal Managers' Financial Integrity Act," NSIAD-84-92, May 1, 1984.

in conjunction with the Office of Personnel Management, is developing a training program which will cover all aspects of the internal control evaluation, improvement, and reporting process. (The first training session was held in March 1984.), and individual agencies have begun developing training materials. The Committee believes that training is essential to assure that managers have a full and consistent understanding of the Act's requirements.

F. AUTOMATED DATA PROCESSING CONTROLS

The reviews of controls over automated data processing (ADP) is another area which also must be improved. Improvements are needed both in identifying responsibility for ADP reviews and in providing additional guidance as to how ADP controls should be evaluated. Generally, agencies did not give full consideration to the review of controls over their automated systems, particularly in the areas of controls over computer software development and data processing center operations.²²

OMB's implementing guidelines state that the controls over ADP should be considered as part of each vulnerability assessment, and identify ADP as an "event cycle"²³ for purposes of agency internal control reviews. This guidance did not, however, result in comprehensive and consistent review of ADP controls. For instance, the Department of Health and Human Services (HHS) did not perform any new vulnerability assessments or internal control reviews of controls in ADP areas; instead the HHS relied on previous assessments of physical security over its ADP operation, in accordance with previous OMB review requirements.²⁴ As a result, HHS did not consider other types of controls in automated systems in its reviews. For example, HHS did not review whether controls were in place to assure accurate, complete, and timely output. HHS has recognized the need to improve its ADP coverage, and reports that policies and procedures to address this deficiency are being developed.²⁵ In another instance, the review process of the Department of Education did not require managers to assess ADP controls as part of the vulnerability assessment process. The Department of Education, however, has indicated it is developing specific criteria that will be used in its internal control reviews of ADP operations.²⁶

Automated systems have gained widespread use and acceptance in the Federal Government. Because of their pervasiveness, and the dependence of the Federal Government on these systems, it is imperative that the agencies clearly delineate responsibility for the reviews required by the Act, and that they have proper and adequate guidance to properly perform reviews of ADP internal controls. The Committee urges agencies to assess the adequacy of their

²² Subcommittee hearing.

²³ The Act's implementing guidelines define an event cycle as the process used to initiate and perform related activities, create the necessary documentation, and gather and report related data.

²⁴ OMB Circular A-71, Transmittal Memorandum No. 1, Security of Federal Automated Information Systems.

²⁵ GAO Report, "The Department of Health and Human Services' First-Year Implementation of the Federal Managers' Financial Integrity Act," HRD-84-47, May 9, 1984.

²⁶ GAO Report, "First-Year Implementation of the Federal Managers' Financial Integrity Act in the Department of Education," HRD-84-49, May 9, 1984.

ADP reviews and to take necessary corrective action to assure that future reviews cover all ADP internal control systems. It also urges that OMB continues its efforts to provide agencies with the guidance necessary to help assure comprehensive and consistent evaluations of this critical function.

G. ACCOUNTING SYSTEMS EVALUATIONS

The final area requiring improvement is the evaluation of accounting systems. As noted earlier, Section 4 of the Act requires each agency head to submit an annual report to the President and the Congress stating whether his or her agency's accounting system conform to the Comptroller General's principles, standards and related requirements.

In the absence of guidance for performing accounting systems reviews, many agencies delayed initiating work in this area until late in the year, and the evaluations that were undertaken were neither comprehensive nor consistent. Several agencies omitted significant accounting operations. For example, several accounting operations at the Department of the Treasury, including the Bureau of Government Financial Operations' check processing system, were not evaluated.²⁷ Furthermore, in those agencies that did assess their accounting systems, the evaluations were based primarily on agency managers' existing knowledge of the operation and adequacy of their accounting systems along with managers' responses to questionnaires or checklists. Agency evaluations did not include procedures to determine whether systems in operation comply with systems as described by managers. As a result, the evaluations conducted could not be used to assure that accounting systems operate in compliance with the Comptroller General's principles and standards and related requirements. For example, at GSA a checklist was developed based on the Comptroller General's principles and standards. The review, however, only covered available documentation; it did not require testing to determine if operating accounting systems actually comply with applicable policies and procedures.²⁸

OMB has advised the Committee that it will issue guidelines covering accounting systems evaluations later this year.²⁹ The Committee expects, therefore, major improvements to be made in this area in future implementation efforts.

VI. POTENTIAL OBSTACLES TO FULL IMPLEMENTATION

In addition to the problems identified during the Committee's review as needing improvement, there are several other factors which may have a future detrimental impact on the implementation and effectiveness of the Act. Federal agency managers should review their ongoing and planned efforts to assure that these concerns do not become major obstacles to the Act's full implementation.

²⁷ GAO Report, "First-Year Implementation of the Federal Managers' Financial Integrity Act by the Department of the Treasury," GGD-84-66, May 25, 1984.

²⁸ GAO Report, "First-Year Implementation of the Federal Managers' Financial Integrity Act by the General Services Administration," GGD-84-57, May 22, 1984.

²⁹ Statement of Mr. Wright, hearing.

A. INCORRECT PERCEPTIONS

The Committee is concerned about comments it has received indicating that some agency officials believe that the first years' implementation efforts have accomplished little beyond merely adding to the paperwork burden on agency managers. These officials have complained that the new process has not identified any problems unknown to managers.

During the subcommittee hearing, Congressman Horton questioned the Comptroller General about the potential for the implementation process to create excessive paperwork. Mr. Bowsher replied that:

... it is important that we get the government systems documented in an efficient manner. Once that is achieved, then the paperwork generated by this review will not be very great . . . I think that this Act actually has the potential for reducing the amount of paperwork in the Federal Government.

The Committee shares this view. While the Act may require documentation which had not been mandated in the past, much of this documentation is an essential part of good managerial procedures. Moreover, implementation of the Act, which provides the necessary discipline for Federal managers to establish, maintain, evaluate and update their internal controls, relies on sound managerial policies and procedures to assure that these controls are solidly based and properly followed. If managers adopt the view that the implementation process is merely a meaningless paperwork exercise, that attitude will hamper efforts to achieve substantial improvements in the management of the Federal Government.

B. INSPECTORS GENERAL ROLE

Although the specific roles played by the individual Offices of Inspector General varied during the first year, their participation in the Act's implementation was important. For example, HUD's Inspector General provided technical assistance to HUD management in the development of the methods and procedures used to conduct internal control evaluations. He also provided an independent assessment, in conjunction with GAO, of HUD's implementation of the Act. In another instance, the Office of the Inspector General at the Department of Education conducted a limited review of management's overall process to implement the Act, evaluated management's internal control reviews, participated in the conduct of six internal control reviews, assigned its Director of Fraud Control to assist in the Department's vulnerability assessment process, and served on the Department's Internal Control Steering Committee. In a third agency, the Veterans Administration, the Inspector General conducted a review of management's implementation efforts, but beyond that, his role was limited to expanding audit plans to provide for greater coverage of internal control issues.

While the Inspectors General represent a valuable resource to managers in implementing the Act, the Committee believes that the Inspectors General must maintain the independence envisioned by the Inspector General Act of 1978. The Act specifically prohibits

an agency head from transferring program operating responsibilities to the Office of Inspector General, and from preventing, or prohibiting, an Inspector General from carrying out any audit or investigation. In addition, the Inspector General, acting on their own accord, must not assume responsibility for managerial or operational functions. This balanced Inspector General role is particularly important in the implementation of the Act in that it appears there are some managers who believe that the Act, given its financially-oriented terminology, is properly the purview of the Office of the Inspector General or equivalent. While the Inspectors General possess unique technical expertise that management should be able to draw upon, the Inspectors General must maintain a proper balance between providing that expertise and their responsibility to independently audit management's programs and functions.

The Committee believes that the Inspectors General can and should review implementation efforts to determine if agencies are complying with the Act's requirements. The Committee also believes that, as the Inspectors General gain experience in this area, their work will increasingly benefit not only managers, but also other entities charged with oversight of agency operations.

C. MANAGEMENT COMMITMENT

Successful implementation of the Act is dependent upon the commitment of managers throughout the Federal Government. Some agency managers have reportedly responded with skepticism and disenchantment as they faced the task of implementing the Act's requirements during the first year, often with limited guidance and support personnel, and inadequate training. One key implementing official has reportedly stated that he hoped the Act's requirements would "die out" before he had to implement them.³⁰ The Committee believes that no amount of after-the-fact auditing or oversight by the Inspectors General, the General Accounting Office, or this Committee can compensate for a lack of management commitment.

Not all agencies have instituted procedures to assure that managers' performance of their internal control and accounting system responsibilities under the Act are properly evaluated. For example, the Navy does not require comments on performance of internal control responsibilities in officers' fitness reports.³¹ The Committee believes that inclusion of managers' responsibilities under the Act in periodic performance appraisals is essential to maintaining accountability and to assuring the integrity of the process required by the Act.

While the relatively good progress agencies made during the first year demonstrates a significant level of management commitment, the Committee urges managers to build upon that commitment. In the future, managers need to assure that performance of the responsibilities required by the Act is evaluated, that detailed internal control reviews and accounting system compliance reviews are

³⁰ GAO Report, "Department of the Navy's First-Year Implementation of the Federal Managers' Financial Integrity Act," NSIAD-84-94, May 1, 1984.

³¹ GAO Report, "The Department of the Navy's First-Year Implementation of the Federal Managers' Financial Integrity Act," NSIAD-84-94, May 1, 1984.

completed, and that deficiencies identified as a result of these reviews are corrected.

D. COORDINATION WITH OTHER MANAGEMENT REFORMS

The first year's implementation of the Act, by highlighting widespread internal control and accounting system weaknesses, has served to elevate concern as to whether the basic structure of the Federal Government's financial management systems is effective.³² Through a disciplined management self-assessment process, the Act has established a basis for identifying and correcting internal control and accounting system weaknesses in individual agencies. These improvements may be of limited utility, however, unless they are directed toward a common set of objectives to improve financial management throughout the Federal Government.

A draft report recently issued by the GAO for discussion purposes, highlights the need for financial management reforms.³³ Programming, planning, budgeting, and accounting systems are often not properly integrated, and they often do not produce reliable information in the form managers need. For example, DOD must prepare its budgets without reliable weapon system cost information. This leads to unrealistic budget planning, difficulties in controlling budget execution, and unreliable information being furnished to the Congress. In the past, piecemeal solutions to these problems have been attempted. The DOD has undertaken several initiatives over the years to address different aspects of the problem of unreliable and inconsistent weapon system cost estimates. Nonetheless, the problem persists. Integrated reforms are necessary in order to achieve comprehensive, lasting improvements.

The Committee recognizes the need for comprehensive financial management reform. However, the Committee believes that these reform efforts must be properly integrated and coordinated with the Act's requirements in order to assure that they are not in competition, or worse yet, in conflict with the much needed agency improvement efforts that are ongoing.

VII. CONCLUSIONS

The Federal Managers' Financial Integrity Act provides the needed discipline for Federal managers to take action necessary to improve management of the government's resources and thereby to increase the American public's confidence in the operation of its government. That confidence has been eroded over the years by disclosures of fraud, waste, and abuse in Government programs resulting from weak internal controls and accounting systems. Federal managers must now systematically evaluate and improve their internal control and accounting systems and submit annual reports on the status of these systems.

Good initial progress was made during the first year in implementing the Act, but much more remains to be done. Agency managers, OMB, GAO and the Inspectors General were all actively involved in the first year implementation efforts. Managers demon-

³² Subcommittee hearing.

³³ GAO Draft Report, "Managing the Cost of Government," AFMD-84-43, March 1984.

strated an increased awareness and understanding of the need for effective systems of internal control and accounting, and began the self-assessment evaluations required by the Act. These assessments resulted in agency heads' generally forthright disclosures of material weaknesses, which form the basis for corrective actions. Many of the problems agencies identified are longstanding areas of concern, but most agencies have just begun the detailed internal control and accounting system reviews that should lead to the identification of many heretofore unknown internal control and accounting system weaknesses.

Several aspects of the implementation process will require improvement if the Act is to be fully successful. In future years, agencies need to assure that all operations are included in the evaluation process; that their evaluation and improvement efforts are adequately documented; that managers receive proper training; and that controls over ADP and accounting systems are adequately evaluated. Both GAO and OMB have already made recommendations for improvements in these areas, and agencies have generally agreed to make efforts to upgrade their implementation activities. Managers need to build on the work done during the first year. They must conduct detailed internal control reviews, and take actions to correct any weaknesses found. In his closing remarks at the subcommittee hearing, Chairman Brooks placed the responsibility for the Act's success or failure squarely on the shoulders of managers throughout the Federal Government:

The ultimate success of the Act depends on the commitment of managers at all levels of government . . .

During the coming years we will be monitoring closely the activities of agency managers to assure that they fully implement the Act.

VIII. FINDINGS

1. Overall, the first years' implementation of the Federal Managers' Financial Integrity Act can be characterized as a learning experience. Managers have become more aware of the need for effective internal control and accounting systems, and some improvement efforts are underway.

2. Agencies did not complete all steps of the evaluation process required by the Act. Consequently, agency heads did not have a sound basis on which to report with reasonable assurance that their internal control and accounting systems are adequate.

3. Many major internal control and accounting system weaknesses across a broad range of government operations, programs, and functions remain uncorrected.

4. Problems have been identified in the implementation process which must be corrected if the Act is to be fully successful. Examples of areas requiring improvement are: guidance, scope of implementation, reporting, documentation, training, controls over automated data processing, and accounting system evaluations.

5. All persons involved in the implementation process must be alert to potential problems that may hamper full implementation of the Act and work toward preventing their occurrence.

IX. RECOMMENDATIONS

1. Federal agency heads should correct problems identified as a result of the first year implementation efforts, including assuring that all programs and functions are covered and that all material weaknesses are properly recorded and reported.

2. Federal agency heads should make a concerted effort to build on the progress made during the Act's first year to complete the evaluation process and to correct internal control and accounting system weaknesses.

3. In order to help assure that Federal agency managers fully understand and properly implement the Act's evaluation, improvement, and reporting requirements, OMB should:

(a) Provide more practical definitions of terms, including "reasonable assurance" and "material weakness"; revise its guidance concerning year-end reporting; and provide guidance for the review of ADP controls and accounting systems.

(b) Continue to closely monitor agency implementation efforts, foster the exchange of information concerning successful implementation approaches, and assure that adequate training is provided.

4. GAO and the Inspectors General should continue to evaluate Federal managers' efforts to implement the Act and the adequacy of agency actions to correct identified weaknesses.

5. OMB and the Executive Branch agencies should assure that current broad-based management reform initiatives, as well as those which may be implemented in the future, are properly coordinated with activities conducted under the Act to avoid conflict or duplication.

A P P E N D I X

An Act To amend the Accounting and Auditing Act of 1950 to require ongoing evaluations and reports on the adequacy of the systems of internal accounting and administrative control of each executive agency, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. This Act may be cited as the "Federal Managers' Financial Integrity Act of 1982".

SEC. 2. Section 113 of the Accounting and Auditing Act of 1950 (31 U.S.C. 66a) is amended by adding at the end thereof the following new subsection:

"(d)(1)(A) To ensure compliance with the requirements of subsection (a)(3) of this section, internal accounting and administrative controls of each executive agency shall be established in accordance with standards prescribed by the Comptroller General, and shall provide reasonable assurances that—

"(i) obligations and costs are in compliance with applicable law;

"(ii) funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and

"(iii) revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the assets.

"(B) The standards prescribed by the Comptroller General under this paragraph shall include standards to ensure the prompt resolution of all audit findings.

"(2) By December 31, 1982, the Director of the Office of Management and Budget, in consultation with the Comptroller General, shall establish guidelines for the evaluation by agencies of their systems of internal accounting and administrative control to determine such systems' compliance with the requirements of paragraph (1) of this subsection. The Director, in consultation with Comptroller General, may modify such guidelines from time to time as deemed necessary.

"(3) By December 31, 1983, and by December 31 of each succeeding year, the head of each executive agency shall, on the basis of an evaluation conducted in accordance with guidelines prescribed under paragraph (2) of this subsection, prepare a statement—

"(A) that the agency's systems of internal accounting and administrative control fully comply with the requirements of paragraph (1); or

"(B) that such systems do not fully comply with such requirements.

"(4) In the event that the head of an agency prepares a statement described in paragraph (3)(B), the head of such agency shall include with such statement a report in which any material weaknesses in the agency's systems of internal accounting and administrative control are identified and the plans and schedule for correcting any such weakness are described.

"(5) The statements and reports required by this subsection shall be signed by the head of each executive agency and transmitted to the President and the Congress. Such statements and reports shall also be made available to the public, except that, in the case of any such statement or report containing information which is—

"(A) specifically prohibited from disclosure by any provision of law; or

"(B) specifically required by Executive order to be kept secret in the interest of national defense or the conduct of foreign affairs.

such information shall be deleted prior to the report or statement being made available to the public."

SEC. 3. Section 201 of the Budget and Accounting Act, 1921 (31 U.S.C. 11), is amended by adding at the end thereof the following new subsection:

"(k)(1) The President shall include in the supporting detail accompanying each Budget submitted on or after January 1, 1983, a separate statement, with respect to each department and establishment, of the amounts of appropriations requested by the President for the Office of Inspector General, if any, of each such establishment or department.

"(2) At the request of a committee of the Congress, additional information concerning the amount of appropriations originally requested by any office of Inspector General, shall be submitted to such committee."

SEC. 4. Section 113(b) of the Accounting and Auditing Act of 1950 (31 U.S.C. 66a(b)), is amended by adding at the end thereof the following new sentence: "Each annual statement prepared pursuant to subsection (d) of this section shall include a separate report on whether the agency's accounting system conforms to the principles, standards, and related requirements prescribed by the Comptroller General under section 112 of this Act."

Approved September 8, 1982.

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